



STATEMENT OF

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TO THE

**COMMITTEE ON POST OFFICE
AND CIVIL SERVICE
HON. WILLIAM D. FORD, CHAIRMAN**

**SUPPLEMENTAL RETIREMENT PROGRAM
FOR FEDERAL EMPLOYEES SUBJECT TO
SOCIAL SECURITY**

**U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.**

APRIL 23, 1985

I am Robert M. Tobias, President of the National Treasury Employees Union. I am accompanied by Paul Newton, our Director of Legislation.

The National Treasury Employees Union is the exclusive representative of over 120,000 Federal employees in a number of Departments and Agencies.

I want to commend the Chairman and members of the Committee for the professional, intelligent and prudent manner in which they have approached this complex and difficult task. The research, studies and hearings conducted by this Committee stand in sharp contrast to the haphazard manner in which proposals have been advanced and changes proposed in the current Civil Service Retirement System, as well as in other areas involving the pay, benefits and working conditions of Federal employees during recent years.

All too often matters concerning the pay and benefits of Federal employees have been discussed, opinions formed and decisions reached in politically charged forums. Fast action and expedient measures designed to help alleviate budget problems have taken precedence over a more rational approach to substantive change in these areas.

We will eagerly work with the Committee to ensure that Members of Congress, the Press and the public understand that the government's retirement system should provide adequate income for employees during retirement. In addition, the new retirement system should serve as a model retirement system for employers nationwide to emulate.

Before turning to the specific areas of interest before the Committee today. I would like to briefly discuss a few issues which we believe are of considerable importance in the development of a retirement plan.

The Federal government is not just another large employer. It is difficult, if not impossible to separate its role as an employer from that of developing and establishing national policies and goals. The retirement plan developed by the Congress will be viewed as government retirement policy and will be emulated by others as such. It is extremely important to establish certain goals and objectives for the new plan that will contribute to the achievement of broader goals and objectives concerning retirement income and security.

Should our goal for retirement be one of enabling those in retirement to maintain their preretirement standard of living; merely meet basic needs; or something in between?

We believe the goal should be that of maintaining their preretirement standard of living.

The President's Commission on Pension Salary in 1981 estimated that the average income replacement that is needed to maintain a preretirement standard of living for a single

person ranged from 79 percent for the minimum wage earned to 51 percent for the highest income person. The range for married couples was 86 percent to 55 percent.

Social Security does not provide sufficient income at any level to maintain preretirement living standards. It is not intended to. As a social insurance program its goal is to provide a floor of income protection.

The employer's (in this case the government) retirement program is crucial if adequate income is to be provided for maintaining a reasonable standard of living in retirement.

Other very important issues to be carefully considered and objectives which must be established are those involving the role the retirement program will assume in personnel management and compensation policy. Should our objective be to provide benefits that will attract and retain quality employees thereby providing the incentive for the development of a well trained, highly competent and dedicated career service? Or should the objective be one of encouraging mobility, and if so to what extent? We believe that the emphasis should be on the former objective rather than the latter.

We also believe that retirement benefits should be formally recognized as deferred compensation, earned by the employee during his or her working career. Our objective should be to provide legal recognition of this and guarantee that the benefits provided and promised at the time of employment will not be subsequently taken away.

When I testified on the supplemental retirement plan at hearings before this committee a little over a year ago, I made some specific statements as to what a new plan should encompass. Very briefly they included the following:

- o The new plan should, in conjunction with social security, provide a level of benefits as close as possible to those under the present system;
- o Some of the major features of the present plan which should be built into the new plan are: basing benefits on high 3 years of salary; protection of benefits against inflation; ability to receive a full annuity at age 55 with 30 years of service, at age 60 with 20 years service and at age 62 with 5 years service; and
- o The financial integrity of the current civil service retirement system must be maintained.

Our views concerning these matters are as strong today as they were a year ago. The rationale in support of them is as valid today as it was at that time.

Cost

We are well aware of the critical role cost will play in determining the design and level of benefits of the new system. We believe that as the new plan is developed and its costs are considered that certain other facts concerning Federal employee pay and benefits should be kept in mind.

This Committee's Hay/Huggins Company Study found that Federal employees were paid 10.3 percent less than private sector employees in 1984. Other studies have shown a higher

percentage. Mr. Shapiro, the President of Hay/Huggins stated in his recent testimony before this Committee that "taking the salary and benefit comparisons together, we estimate that private sector total compensation exceeds that of the Federal government by more than 7 percent. And, after the moderate 3.5 percent Federal pay increase this past January, we expect to find an even wider gap. . .this summer." If there is no pay increase at all for 1986 this gap would not only be considerably greater but could only be considered horrendous.

The extent to which the design of a new plan achieves the basic objectives of providing adequate income at retirement and attracting and retaining quality employees, certain cost savings will be achieved in the areas of reduced training costs, higher productivity and improved quality of work.

Mr. Chairman, in considering this complex and highly charged subject, we believe that it is absolutely essential that only one cost model be used as a basis for comparing existing and proposed retirement plans. One common set of assumptions or a single basic line, if you will, that can be used throughout the legislative consideration and deliberation of alternative designs. Such a cost model has been constructed by the Congressional Research Service in preparing their report "Designing a Retirement System for Federal Workers covered by Social Security."

We recognize that the "entry-age normal cost" expressed as a percentage of payroll is a generally accepted measure for estimating the long term cost of a retirement system. It is not a precise or exact measure of the cost. It will be so only if the assumptions on which it is based match exactly

the actual conditions that occur in the future. We know of no better method for estimating cost, and find the normal cost method very appropriate. The employer cost of the new plan including Social Security should not exceed the cost of the current system.

Social Security Tilt

The Social Security "tilt", the problem it presents and the reasons these problems exist have been described and discussed at earlier hearings. They have also been explained in considerable depth in studies prepared for the Committee and for other purposes.

Basically there are three methods for designing a new retirement plan that will be coordinated or integrated with Social Security. They are usually referred to as the add-on, offset and step rate methods.

The add-on method is one in which the formula would provide benefits based on years of service and salary. These benefits would merely be added to the Social Security benefits. It ignores the "tilt" and therefore the effect of the social security tilt is carried over into the overall retirement benefits received by employees. Lower paid, married and shorter service employees will have higher income replacement rates than higher paid, single and long service employees.

Under the offset method, the formula is designed in a way to partially offset the benefits provided by Social Security.

The step rate method formula is designed in a way that a different percentage would be applied to various levels of pay. A given percent would apply to pay up to a certain amount and a higher percent to pay above that amount. It produces different income replacement rates for employees with the same service when their salary is different.

Both the offset and step rate methods reduce the effect of the Social Security tilt. ERISA and IRS regulations do not permit private sector plans to completely offset Social Security benefits. While the regulations are not applicable to the Federal government we believe that as a matter of public policy they should be followed in the design of the supplemental plan. Thus, only half of the Social Security benefit could be offset. This still would leave a difference in income replacement rates between the lower paid and higher paid employees. However, these differences would only be about half the level they would be under the add-on method.

The offset and step rate methods of integration with Social Security are the ones most commonly found in the private sector.

We believe that the new plan should use either an offset or step rate method. The step rate method would probably be the most equitable to achieve the goal of more consistent income replacement rates.

Employee Contributions

Employees hired since January 1, 1984 are now required to pay the social security tax. The total tax in 1985 is 7.05 percent of pay up to \$39,600. Of this amount, 5.7 percent is for the Old age, Survivors and Disability Insurance provided

by Social Security and 1.35 percent is for Medicare. In 1986 the total tax will be 7.15 percent due to an increase in the Medicare portion to 1.45%. In 1988 it will be 7.65 percent due to increases in the OASDI portions to 6.06 and to 6.2 percent. The salary base on which the tax is paid will also increase and is estimated to be \$50,700 by 1990. For most employees this is a substantial amount.

Although employees pay the Social Security tax, in the private sector the prevalent practice is that the employer pays the full cost of the supplemental retirement plan.

Employees covered under the current Civil Service Retirement System contribute 7 percent of salary to the Retirement Fund. They are not covered under Social Security, but they are required to pay the 1.3 percent tax for Medicare coverage.

Requiring higher contributions than those in the existing program would not only cause financial hardship to most employees but would adversely effect the Government's ability to recruit and retain quality employees. It is our view that employees should not be required to contribute to the new Supplemental Retirement Plan.

A capital accumulation plan should be an integral part of a retirement system above and beyond the basic goal of providing for a preretirement standard of living. The benefits from a capital accumulation plan should be at the employee's option to increase their retirement standard of living or for other purposes and not be calculated as part of what is necessary to maintain retirement income security. Those who cannot afford or do not want to participate in a

Vesting

The original Civil Service Retirement law provided for full vesting after 15 years. In 1942 the current 5 year vesting provision was placed in the law.

ERISA regulations do not permit employees in the private sector to have a vesting provision of more than 10 years. Most private sector employers use a 10 year period for their deferred benefit plans.

Closely related to the issue of vesting is the one involving portability. Under the existing retirement system there is very little portability of earned benefits. A vested employee who leaves government service is entitled to a deferred annuity at age 62 or to a refund of his or her contributions. Most of these employees choose a refund of their contributions rather than waiting years to receive the deferred annuity. By doing so they forfeit valuable retirement benefits and receive no benefit from the government's contributions. In terms of building retirement income, these years are lost.

Since new employees are covered under Social Security which is portable this problem is alleviated to an appreciable extent. If a Capital Accumulation Plan is established, these benefits would also be fully portable. We recommend, that the portability of the supplemental plan follow the prevailing private sector practice, which generally provides for deferred benefits accruing at the age of retirement or a pay-out on termination of employment, if the value of the annuity benefit is below a specified level.

We recognize that the personnel management goals that are established for the system can and should influence the selection of the vesting period. Cost is also a factor to be considered.

Presently, we see no compelling reason for a vesting period longer than that under the current system, which is five years.

Funding and Financing

There are several methods which the Federal government could use to finance the new retirement plan ranging all the way from full funding to pay-as-you-go.

Since its inception the current Civil Service Retirement System has been financed in a number of ways. Employee contributions were the sole source of funding for a number of years; employee contributions and appropriations from general revenues were used; then employee and agency matching contributions; and finally in 1969 the current funding method was established. The 1969 financing method of employee and agency matching contributions, with an appropriation to match costs as they accrue, served the purpose of insuring that the Retirement Fund would be able to provide benefits to present and future retirees as they became due.

The Social Security System is financed on what might be call a "generational" basis. Today's employers and employees provide the funds to pay the benefits of today's retirees. The contributions are set to meet this benefit cost and to

provide an amount above that to maintain a Trust Fund at a level to meet certain contingencies that may occur in the future.

The Military retirement system has been financed on an annual pay-as-you-go-basis.

The Employer Retirement Income Security Act sets minimum standards for funding private sector pension plans. These standards require annual contributions equal to the normal cost plus amortizations over 30 or 40 years of unfunded accrued liabilities for all plan benefits.

The most important purpose served by the financing method used is that it insures that the employees covered by the plan will receive the benefits the plan provides. There are other very important purposes that should also be served by the financing method used. It should recognize costs as they are incurred. The employees covered by the plan will feel secure and confident that a Fund exists at an adequate level to provide for their retirement benefits as promised. Pay-as-you-go funding which would be dependent on annual appropriations would not serve these purposes.

Unique Employment Categories

Mr. Chairman, although your letter concerning this hearing stated that at a later hearing you would be considering how certain groups such as law enforcement officers, firefighters and others should be treated under the new plan, I appreciate you affording me the opportunity to testify concerning this matter today, I will attempt to be as brief as possible.

The National Treasury Employees Union represents many individuals who are currently covered and who receive benefits under the special provisions of the retirement law that are applicable to law enforcement officers. These include Special Agents of the Internal Revenue Service, Special Agents and Patrol Officers of the U.S. Customs Service, Special Agents of the Bureau of Alcohol, Tobacco and Firearms. NTEU also represents other groups including both Customs Inspectors and IRS Revenue Officers, who by the very nature of their duties should be covered under these provisions but have been denied benefits based on a technicality in the law.

The reasons for providing special retirement treatment for law enforcement officers that existed at the time they were placed in the current law are even stronger today. They should be treated no less favorably under the new retirement plan. The plan must not only provide for early retirement but insure that it is economically feasible to do so. Since Social Security will not be payable until age 62 it will be necessary to supplement the basic benefit provided by the new plan for the years between the age they are at separation and age 62.

The development of a new retirement plan provides an opportunity for Congress to clarify and correct certain problems and inconsistencies that exist in the current law and at the same time provide for similar treatment of employees engaged in similar work under the new law. The provision

concerning coverage of law enforcement officers was initially enacted in 1947. It was primarily written to cover F.B.I. agents. It was amended five times between 1947 and 1974 to cover certain other occupational groups. As a result the broad occupational category of the position occupied became paramount rather than the actual requirements and duties of the positions occupied.

The duties and responsibilities of both Customs Inspectors' and IRS Revenue Officers' more than meet the criteria established for coverage under the special provisions for law enforcement officers coverage. However, because of one word in the current law they have been denied these benefits. Their positions are not considered as "primarily the investigation, apprehension, or detention of individuals suspected or convicted of offenses against the criminal laws of the United States. . .". (emphasis added), yet by every other measure, the positions require the same degree of "law enforcement" background and exposure to hazards as other police type functions which do qualify. Custom Inspectors today, for instance, are making an increasing number of arrests and are not allowed to perform inspector duties until qualified in firearms. Kidnaping, murder and assaults are an ever present danger in both professions. More and more Customs Inspectors are working on Special Enforcement Teams doing undercover investigatory work with Special Agents, Drug Enforcement Agency personnel and local law enforcement groups to stop the increasing flow of

drugs into this country. Similarly, IRS Revenue Officers are exposed to an ever increasing number of life-threatening situations in the course of their normal duties. Assaults against IRS employees increased from 531 in 1983 to 789 in 1984 -- a 50 percent increase. In addition to these incidents, there are several well-financed groups around the country who advocate organized violence against IRS employees. Excluding these occupational categories is not only unfair to this group of employees but prevents the government as employer from maintaining a young and rigorous workforce in this vital area of law enforcement.

Thank you very much, Mr. Chairman, that concludes my testimony this morning. I would be happy to answer any questions you may have.